

# Piracy and the U.S. Economy

An address given to the Los Angeles World Affairs Council  
on, October 25, 2006 by Bob Wright, Chairman and CEO, NBC Universal

Everyone here knows piracy is a big problem for the media and entertainment industry. We are devoting enormous resources toward this issue. The Motion Picture Association of America (MPAA) spends millions of dollars a year. Media companies spend millions more on their own.

If there is lack of understanding on this issue, it's *outside* the media industry. It lies with politicians, policymakers, and the public. They need to understand what we're facing. They need to be educated and motivated to take action. And the burden is on us to do this.

I want to suggest what I think is the *only* way to gain traction on this issue with people beyond the film industry. We need them to understand that the impact of piracy and counterfeiting goes far beyond the economics of movie and music companies. We need to convince them that film and TV piracy affects not merely content companies but a wide swath of economic activity—to the tune of \$20 billion a year—that contributes to, and benefits from, the production and distribution of films. We also need to convince them that piracy affects a wide range of other sectors, with grave ramifications for our overall economic health and future growth.

That message needs to be articulated as forcefully and clearly as possible. Because as long as piracy is downplayed in the public mind as kids downloading music from the Internet, we won't get the energy and focus we need.

The good news is that we have more and more data to help back up our position. I will talk about this in a few minutes. But, standing here at the heart of the creative community, I want to encourage an even more vigorous partnership to raise the profile and the temperature of the anti-piracy issue.

John Updike recently spoke out about what he called the "grisly scenario" if "freely flowing snippets" of written works proliferated without limit on the Internet. The voices of creators—actors, writers, producers, directors—stand out above the din and command attention and respect. They need to be heard.

I was in Washington last month to speak to business leaders and government officials at the U.S. Chamber of Commerce. My goal was to unveil some new data and thereby raise the level of knowledge and concern about piracy and counterfeiting among what you might call "the suits." Today, standing in the world's creative epicenter, my goal is the same.

As I discuss my perspective on this issue, it is my hope that all participants in the media business will join together to carry our anti-piracy message to the public, to elected officials, and to our partners.

For those of you who are in the film or TV industries, I'd like you to think for a minute about the future of your business.

The DVD market—so important to movie studios for the past few years—is maturing. We're seeing price erosion, flattening penetration, and slowing sales growth. Domestic box office was down last year. The revenue stream of film sales to TV networks is under pressure. Production and marketing costs continue to climb, to an average of nearly \$100 million per film last year.

I could paint just as gloomy a scenario in TV, if I wanted to. Network and local TV stations' ad revenue is weakening. The syndication marketplace is flat. DVR penetration is growing, leading to contentious debates about audience measurement and metrics for advertisers.

I know, I'm making media sound like American steel after World War II. But let me be clear: Hollywood is *not* Bethlehem, PA. We have *huge* opportunities for growth. For growth internationally, as we expand the delivery of our content to new markets, and growth digitally, as we expand *how* we deliver content to consumers.

I'm sure you can guess where I'm heading ... Yes, our two areas of growth—international and digital—are *exactly* the ones most impacted by piracy.

China has 1.3 billion people and a piracy rate of more than 95percent. That means that out of every 10 DVDs viewed by consumers in China, perhaps one is purchased through legitimate channels. If we can reduce piracy and government limitations on exhibition of non-Chinese movies, China has enormous potential, especially with a rapidly growing middle class that in a few years will be as large as the total population of the United States.

But it is hard to compete with free. It's hard to compete against the teenager in Beijing who spends hours every week downloading illegal copies of American TV shows, adding subtitles, and posting episodes on the Internet. It's hard to compete against the sophisticated, well-organized groups that produce, market, and distribute illegal, high-quality DVDs of movies before they even hit the screen.

Meanwhile, Russia has an 80 percent piracy rate, with the same sort of activities. In countries like these, it's virtually impossible for legitimate business to even get a foothold.

In countries where we have already developed robust businesses, we're seeing serious erosion in our established positions. In Mexico, the piracy rate has exploded to more than 60 percent of the market. According to the MPAA, this represents losses to member

studios of nearly half a billion dollars a year. In Great Britain, the piracy losses amount to more than \$400 million.

I don't need to convince this audience that media companies are taking a big financial hit from piracy and counterfeiting.

But let's broaden the discussion. Any healthy society rests on two strong pillars: physical security and economic security.

We all know that our physical security has been threatened for the past five years. But our economic security is also being challenged. It's being challenged by piracy and counterfeiting.

It is interesting that when I suggested this to some of my colleagues at NBC Universal, I was accused of being melodramatic. Wasn't I overdoing it a bit?

To which I responded: No, I'm *not* overdoing it and furthermore, this perfectly illustrates my point! If people whose livelihoods are on the line don't get the extent of the piracy threat, then we really *are* in a state of denial.

Although no one could equate the horrific loss of life we've suffered in the war on terror with the economic losses coming from piracy, I do want to suggest that we are indeed under economic attack by piracy and counterfeiting, across all sectors of our economy, with enormous implications for our future.

The U.S. economy is threatened by increases of counterfeiting and piracy in sectors as diverse as automobiles, aerospace, computer software, defense contractors, fashion design, high-tech manufacturing, and pharmaceuticals. At risk is every part of our economy where creativity, innovation, and invention drive the creation of economic value and of high-wage jobs.

So what is our response to this threat?

I want to suggest four steps that will lead to real progress in this battle.

First, we need to recognize the impact piracy and counterfeiting have on our economy today and the threat they pose to our future. We need to understand that it cuts across all business sectors. And we need good data to quantify the costs.

Second, leaders in every sector, and especially the media, must use all their powers of persuasion to get the message out that piracy and counterfeiting are serious crimes. This isn't a problem of one or two sectors or a few big companies. We're talking about organized crime. And we're talking about the future economic security of our nation.

Third, we must significantly increase resources at all levels of government, in this country and globally, to enforcement against intellectual property crime.

And fourth, especially in media, which has such a high profile, key players in the private sector must take steps within their control to reduce piracy. We must collaborate, public and private, and across industry sectors, with special attention to technological solutions.

Now, let me elaborate a bit on each of these four prongs of attack. First, we must recognize the cost.

First, recognize the cost. Last year, NBC Universal commissioned a study from economist Steve Siwek entitled *Engines of Growth: Economic Contributions of the U.S. Intellectual Property Industries*. The study was designed to answer an important question: How dependent is our economy on those industry sectors that are driven by innovation, invention, and creativity?

The Siwek study aggregated the intellectual property (IP) industries—industries that rely heavily on copyright or patent protection—and measured their revenue, employment, compensation to workers, and growth.

It found that these industries are the most important growth drivers in the U.S. economy, contributing nearly 40 percent of the growth achieved by all U.S. private industry and nearly 60 percent of the growth of U.S. exportable products and services.

*Engines of Growth* put some numbers on what was already quite evident: IP industries are our economic future. These sectors are the driving force behind our ability to sell goods and services around the world. And they are being seriously damaged by piracy. But what does this mean specifically in terms of lost output, lost jobs, and lost tax revenues?

We decided to try to make progress toward solving this puzzle, starting with the movie sector.

The Motion Picture Association of America had recently completed a comprehensive study of global movie piracy, which established that the six MPAA companies lost \$6.1 billion to worldwide piracy in 2005.

When a studio loses revenues to piracy, it doesn't have that money to reinvest into making more movies and television. Not only does this affect the individual studio, but it impacts all the companies that would have contributed to or benefited from these unmade productions, and the creative people who work for those companies. It reduces the revenue both of the upstream suppliers of entertainment products, and of the downstream industries, like movie theaters, DVD retailers, and video rentals.

How can these losses be measured? The U.S. Department of Commerce, through its Bureau of Economic Analysis, has developed a method of measuring these cascading effects. It uses what are called "input-output multipliers" to quantify how much the change in the output of one industry will change the output of other, related, industries.

The Institute for Policy Innovation, a think tank based in Texas, commissioned a study that applies these analytical tools to the MPAA's data on piracy.

The IPI study found that the \$6.1 billion the MPAA identified as lost to piracy actually translated into total lost output among all U.S. industries of \$20.5 billion annually.

In addition:

- Motion picture piracy costs U.S. workers \$5.5 billion a year in lost earnings; two-thirds of which would have been earned by workers in other U.S. industries.
- Absent piracy, 141,000 new jobs would have been added to the U.S. economy.
- And finally, motion picture piracy costs governments at all levels, conservatively, \$837 million in lost tax revenue.

This study starts to indicate how damaging the true cost of piracy and counterfeiting is—and its focus is just one industry. Imagine if we included the losses of other industries that are hit hard by IP theft, such as software, luxury goods, and automotive parts. The numbers would be staggering.

For example, the software industry conducted a study recently and concluded that a 10-point drop in the global piracy rate in their industry would yield 2.4 million new jobs and \$400 billion in economic growth over four years. It is clear we are talking about hundreds of billions in lost productivity and many millions of jobs.

Today's public policy debates have not benefited from a documentation of the overall impact of these crimes on our economy. A full accounting would galvanize a far greater appreciation of the extent to which our economic security is at stake.

My second point is that we need to do a better job of communicating how important this issue has become. We have a responsibility to convey to our customers and constituencies that intellectual property rights are vital to our economic future.

We need to call upon private industry to step up worldwide campaigns to educate consumers and policymakers about the moral and economic reasons to protect intellectual property. We need to call upon the administration to ensure, in its negotiations with trading partners, that it makes the case that this is an economic security issue. We need to call upon our elected representatives to keep the spotlight focused on our economic security. We need to call upon both political parties, as the election season draws near, to make IP protection a centerpiece in the effort to keep the U.S. competitive. And we need to call upon the creative community to recognize that this isn't someone else's issue to deal with; it is yours.

My third prong is enforcement. This is a time of constrained resources. But failing to act is penny wise and pound foolish, because future tax receipts will more than offset today's enforcement expenditures.

Whether it is a counterfeit drug, a computer-generated car design, the theft of a valve technology from a French industrial parts supplier, or a pirated copy of *King Kong* distributed online, counterfeiting and piracy must receive priority enforcement attention.

The media sector, of course, faces special challenges. Technology makes it easier than ever to illegally distribute copyrighted materials to millions of people from anywhere in the world. This makes enforcement efforts at once more difficult and more important. At the federal level, we've seen the Department of Justice increase its resources in this area significantly. But Congress needs to act this year to appropriate funds for significant increases in FBI investigative resources devoted to IP crime.

We need more resources at the Department of Homeland Security dedicated to stopping counterfeit and pirated goods at the border. We need more enforcement resources at the state and local levels. Overseas, the U.S. must continue and step up efforts to ensure that our trading partners—including Russia and China—respect and enforce intellectual property laws.

It is not a hopeless situation. Where there is the political will, the tide can be turned. Taiwan and Hong Kong, for example, have made good progress since their governments made strong enforcement a serious priority.

Fourth, we need cooperation within and across sectors. We need all industries to be committed to taking action in areas that are under their control and also to support wider public policy efforts. We should recognize, too, that effective solutions will require a heavy measure of technology.

The media industry has long been criticized for resisting technology and protecting old business models. Today, nothing could be further from the truth. We and our competitors are embracing new digital delivery systems as quickly as they appear.

We are entering an era marked by an incredible wealth of video choices at your fingertips. All this has a dark side, however. It makes our most valuable products incredibly vulnerable to theft.

We need our business partners to be as aggressive in deploying technology for fighting theft as they are in deploying technology for new digital distribution.

It is ironic that some of the very same parties who suggest content companies aren't moving fast enough to embrace new distribution technologies, fail to call on technology and distribution companies to accelerate the development of technology to fight piracy.

It is terrific that ISPs are investing billions to roll out broadband services. Yet independent firms report that well over half of broadband traffic is devoted to peer-2-peer file sharing, which is dominated by the illegal exchange of movies, music, software and games, not to mention pornography.

We need ISPs to work in partnership with content companies, passing notices to and, if necessary, terminating relationships with customers who abuse their networks. Moreover, ISPs and content companies should be working together to develop ways to filter out illegal content while speeding along legal content. This is an acute issue on college campuses, where students use ultra-fast computer networks for illegal downloading more than for academic research.

We need university administrators to take much stronger action, including the use of blocking technologies, to stop wholesale illegal downloading on campus. Their action or inaction sends an important message to students about whether illegal activity is condoned or condemned.

The fact is, technological steps that would significantly reduce much of the piracy problem for media companies are available right now. We have the ability to insert a digital “tag” or “watermark” in our content. The CE, IT and content industries have cooperated in developing technological standards for the new HD generation of DVDs, which will include provisions for detecting copyright watermarks in order to interfere with the playback of pirated material.

This is a welcome development. But it is absolutely critical that we continue down this path. We need our business partners to help us apply the same technology to the new tools that will facilitate moving digital material from device to device within the home; from computers to handheld devices to TV sets.

I’ve discussed four steps that will lead to progress on this issue. By way of conclusion, let me suggest four specific things I would like to see happen over the next 12 months.

First, we need to have hard numbers on the table that reveal the full impact of piracy and counterfeiting on our economy. The IPI study is a great start but it needs to be expanded and complemented by other studies, in industries from fashion to pharmaceuticals. That is going to take a commitment of resources and data from government and from other business sectors.

Second, we need to see stepped-up advocacy by both the private and public sectors. On the private side, this means companies in every sector, from aerospace to automotive, working together with organizations like the Chamber of Commerce’s Coalition Against Counterfeiting and Piracy, and the International Chamber of Commerce’s Business Action to Stop Counterfeiting and Piracy, to convey the scope of the problem. On the government side, it means clear pronouncements from the administration, Congress, and both political parties that our future growth depends on rigorously protecting intellectual property.

Third, law enforcement at the federal, state, and local levels needs to be in a much better state of readiness, with adequate resources in place. Congress should follow through on the effort to add 65 agents at the FBI and Customs dedicated to IP crime, in sectors ranging from financial services to manufacturing. I would also call on the governors and

attorneys general in our ten largest states, and the mayors and chiefs of police in our twenty largest cities, to adopt coordinated, model IP protection enforcement programs in their jurisdictions. We need more cities to follow the lead of New York, which on Monday announced a stepped-up campaign against video piracy.

Fourth, we need to make real progress in implementing technological solutions. In our own industry, I hope we are well on the way to partnering with the CE, IT, and ISP industries, as well as the university community, and putting serious resources and effort into implementing technological solutions that create real roadblocks to the digital distribution and playback of pirated products.

I began these remarks with a reference to Bob Woodward's latest book, which draws some strong conclusions about the state of our nation's physical security. What we know now is that our *economic* security rests on the shoulders of the intellectual property industries.

The author Richard Florida has written: "The ultimate intellectual property—the one that really replaces land, labor, and capital as the most valuable economic resource—is the human creative faculty." The creative faculty is what makes Hollywood unique. It entertains millions around the globe. It educates and inspires. And it is a major part of the linchpin of our economy.

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